Intelligence MEMOS

From: Lawrence Herman

To: Canadians Concerned about Trade Disputes

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Re: **IT'S TIME FOR CORPORATE TRADE-RELATED RISKS TO GET FULL DISCLOSURE**

It's now widely agreed that the global trading order has been shattered, led by aggressive actions under Donald Trump's America First policy. With national security as the rallying cry, tariffs have been weaponized, starting with US surcharges on steel and aluminum, and extending into other areas.

Governments, including Canada's, responded with countermeasures of their own on US goods. The spectre of US surcharges on autos and auto parts continues to overhang global markets, along with the threat of additional tariffs on Chinese products beyond those currently hit and the likelihood of Chinese responding in kind.

Compounding these unilateral developments, the World Trade Organization's dispute-settlement system is paralyzed because of US refusal to agree to appointments to the WTO Appellate Body, making it impossible for disputes to be judicially resolved by that organization. The International Monetary Fund, the World Bank, the Organisation for Economic Co-operation and Development, and the Bank of Canada have warned repeatedly about the negative impact this is having on the global economy.

In spite of this heightened concern, relatively little attention has been given by the investment community or by industry regulators, including in Canada, to the need for disclosure of trade-related risks in corporate reporting. Contrast this with the climate-change situation, where risk disclosure in a world shifting to a low-carbon future is the accepted standard for public corporations.

One of the underlying reasons is to limit litigation exposure. A 2019 Mercer LLC report speaks about ever-increasing lawsuits aimed at companies failing to mitigate, adapt or disclose these environmental risks, including litigation against governments and, most recently, pension funds.

In May, 2019, the United Nations Environment Program engaged a collection of institutional investors from 11 countries, launching a comprehensive guidance program to assess how climate change and carbon-emission actions could affect investor portfolios and how corporations would need to deal with this.

The G-20's Financial Stability Board under former chair, Mark Carney, created a Task Force on Climate-Related Financial Disclosure (TCFD), to monitor and encourage greater corporate climate risk disclosure.

At home, the Canadian Securities Administrators issued CSA Staff Notice 51-358, its guidance to assist public companies and their boards in assessing the materiality of environmental risks, and requirements of full and frank public disclosure of those risks.

With intensified reporting obligations regarding climate-related risks and the impact of carbon-pricing on corporate performance, why isn't more attention being paid to trade-related risks?

Sectors such as steel, aluminum, automobiles, agriculture and other internationally traded products are among the most directly affected by national protectionism, including import restrictions, discriminatory preferences, unilateral surcharges and tariff hikes. While these kinds of trade risks are being reported in some sectors, some are more complete than others.

In the softwood lumber sector, for example, there's a fair degree of risk-assessment disclosure about the damaging influence of US countervailing duties. Even here, discussion is ad hoc with no set guidelines or reporting standards. In other sectors, such as automotive, trade risks often get just cursory notice in annual and quarterly reports.

Given the damaging impact of all forms of trade protectionism, it would seem reasonable for standards to be developed so that corporations will disclose, review and put a price on some of those trade-related risks in a more organized and informative fashion. Elements and disclosure protocols can be derived from the CSA Staff Notice. For example:

- In business sectors most exposed to disruptive trade measures, boards could adopt a planning process, in combination with an oversight mechanism, to provide early warnings of potential foreign government actions.
- Once identified as material ("materiality" being the critical factor), those risks could be scrutinized by board committees, paving the way for management's discussion and analysis in quarterly and annual reports.
- Trade-risk identification could include such things as exposure to anti-dumping and anti-subsidy actions, protectionist measures such as safeguards, as well as embargoes and trade sanctions restricting transactions in specific markets.

The point of all this is that, given the profound impact protectionism and other trade measures have on international business, more robust disclosure standards and best reporting practices are worthy of development, all to the benefit of investors.

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